

# **Risk, Positive Integration and System Friction: The Single European Market and World Trade<sup>1</sup>**

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<sup>1</sup> Earlier versions of this paper was presented at the 13th International Conference of Europeanists, Chicago, 14-16 March 2002 and the 52nd Political Studies Association Annual Conference, Aberdeen, 5-7 April 2002. It draws on several earlier research projects, and I would like to thank my collaborators on those projects, especially Peter Holmes, Chris Stevens and Helen Wallace. It also draws on work that I did while a Jean Monnet Fellow at the Robert Schuman Centre, European University Institute (2000-01). I would also like to thank Greg Shaffer and David Vogel for their comments on an earlier version. All remaining short-comings are my own.

## 0. Introduction

Domestic regulations are becoming an increasingly important, albeit usually unintentional, source of international trade friction. The European Union's single European market (SEM) programme is the world's most ambitious attempt to remove such barriers between countries. Although the EU's project of internal liberalisation has generally benefited third-country firms as well, some modes of market integration can create barriers to imported goods. Where trade barriers are due to fundamentally different regulatory approaches, they can be thought of as a form of 'system friction' (Ostry, 1997: 98). For both political and legal reasons, such barriers are particularly difficult to resolve within the multilateral trading system. As a consequence, background trade friction may become a persistent feature of international trade. That, however, may be no bad thing.

In this paper I connect two usually distinct features of (and literatures on) the SEM: its internal dynamics and its external impact. Specifically, I argue that EU rules that impede international trade are most likely to occur where differences in regulatory approaches among the EU's member states are sufficiently pronounced that common rules ('positive integration')<sup>2</sup> are necessary to overcome trade barriers among the member states. In such circumstances, the dynamics of integration tend to push towards stricter standards, what David Vogel (1995: 8) has called 'trading up.'<sup>3</sup>

Because the adoption of common EU rules tends to imply a more restrictive approach, it creates barriers to foreign goods. The ensuing trade tensions, I argue, are particularly difficult to resolve within the multilateral trading system because the World Trade Organisation (WTO) accepts as legitimate some limits on free trade, but lacks the institutional structure for agreeing common rules. Further, the rules in question tend to be politically sensitive and reflect difficult internal compromises. As a result, they are difficult to change, even under the threat of WTO approved sanctions.

Although this paper focuses on the 'obstacles' to integration within the EU and in the multilateral trading system, I do not mean to detract from their major accomplishments. Rather, I argue that these trade frictions are actually a symptom of a necessary political condition for integration: acceptance of legitimate differences. Consequently, this paper suggests that common concerns that the WTO fundamentally threatens national regulatory autonomy are overstated.

The rest of the paper is in six sections. The first three provide background information: the first describes the significance of the EU's regulatory trade barriers; the second explores on the challenges of addressing regulatory trade barriers; and the third discusses the methodological issue of identifying disputes. The fourth section picks up the first portion of my argument and examines the dynamics of market integration within the EU. In particular, I explore the implications of the different approaches to market integration employed by the EU for third-country firm market access and describe how the dynamics of market integration shape both the choice of mode and the strictness of any common rules. The fifth section assesses how well

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<sup>2</sup> Tinbergen (1954: 122) considers 'positive integration' the adoption of common rules. Pinder (1968: 90) also stresses that the purpose of the measure should also be to maximise welfare, not just remove discrimination. My usage clearly fits with Tinbergen's usage, and, I would argue, with Pinder's.

<sup>3</sup> The use of stricter standard here does not imply that stricter standards are objectively better. Stricter standards imply costs that may not be justified by the risks addressed. Likewise stricter standards may address some risks while heightening others.

equipped the multilateral trading system is for helping to resolve the resulting trade disputes. In the final section I conclude by drawing out the implications of my analysis for the future of the multilateral trading system.

In order to keep the narrative manageable, I focus primarily on the transatlantic economic relationship. This focus is justified by the United States being the EU's main trading partner; by the US government being the most prolific user of the World Trade Organisation's Dispute Settlement Mechanism; and by the ready availability of information.

### 1. The increasing significance of regulatory barriers to trade

The crowning success of the multilateral trading system has been the significant reduction in at-the-border barriers to trade -- tariffs and quantitative restrictions -- especially in industrial products. As a consequence of multiple rounds of multilateral negotiations, even US industrial exports, which along with those of six other countries enter the EU without preferential treatment, face an average tariff of only 4.2 percent and 20 percent of tariff lines enter duty free (WTO, 2000a: 7-8). Although the EU's simple average tariff on agricultural products is significantly higher at 17.3 percent (WTO, 2000a: 8), access on high-tariff items takes place mainly through tariff quotas (much lower tariffs apply to in-quota imports).

As tariffs have fallen and quantitative restrictions have been eliminated, regulatory barriers to trade have become more prominent (OECD, 2000; PIU, 2000; World Bank, 2000). The EU's regulations and standards now represent the most significant barriers to market access (USTR, 2001: 108; WTO, 2000a: 8).

### 2. The challenge of removing regulatory barriers

Eliminating regulatory barriers to trade, however, is fundamentally more challenging to national autonomy than reducing tariffs, because most regulations serve legitimate and necessary purposes unrelated to trade. Consequently, they cannot simply be swept aside. Squaring the circle by replacing diverse national rules with common rules is fiendishly complicated and time-consuming.

The problem exists because there are a number of legitimate reasons for national regulations to diverge (Hancher and Moran, 1989; Previdi, 1997). First, and most straight forward, different countries face different problems. This naturally results in different policy responses. Usually the policies that address such problems regulate production processes rather than product characteristics and so do not normally impede trade.

Second and more fundamental, there are cultural differences in attitudes towards risk, often shaped by experience (Isaac, Banerji and Woolcock, 2000). In the EU the recent experiences with government mishandling of the BSE crisis (the UK and elsewhere), HIV-tainted blood (France) and dioxin-contaminated food (Belgium) have been formative (Pollack and Shaffer, 2001; Vogel, 2001). When devising product-safety rules no formula will be perfect. There is the double-edged risk of mistakenly banning something that is quite safe or of mistakenly permitting something dangerous. The trade off depends on subjective preferences regarding the consequences of error, and national regulatory frameworks will be set such as to opt for more of one or other risk (Holmes and Young, 2001a). It is worth noting, that such cultural differences seem to matter most when it comes to deciding how much risk to accept and how to manage it, rather than how to assess the level of risk (Council, 2000; Woolcock, 2002).

Third, even if two political systems face the same problem and have the same attitude to risk, politics might well produce different outcomes (Hancher and Moran, 1989; Pollak 1998). As different political systems

have different constellations of societal interests and different political institutions, the political interplay between them would be expected to produce different regulatory outcomes.

Given the numerous legitimate bases for differences in national regulatory approaches, the question arises how to cope with the tension between trade liberalisation and regulatory autonomy (Jackson, 1997). The EU and the multilateral system both face trade offs between the risks of allowing national bans that are ostensibly for consumer protection, but actually are sheer protectionism (letting a guilty person go free) versus the danger of preventing governments banning products merely because their collective preferences are different (convicting an innocent).

### 3. What is a dispute?

Although it is easy to recognise that regulatory barriers can impede trade, a crucial and vexed question for analysing the origins and resolution of actual disputes is how to identify systematically trade disputes. A common classification uses the formal request for consultations within the GATT/WTO (see, for example, Hudec, 1993). This has the big advantage that the information is readily available and is, within limits, comprehensive. Those limits, however, mean that the information is subject to selection bias as a large number of disputes never make it as far as formal consultations (Busch and Reinhardt, 2002). As my specific focus is on the impact of the single market programme, I omit cases against individual EU member states. It should be noted that some issues, such as the EU's ban on hormone-treated beef and banana trade regime, have been the subject of multiple cases (see Table 1).

[Insert Table 1 about here]

Although gathering information on disputes that are not the subject of formal dispute resolution is normally problematic, the United States Trade Representative (USTR) publishes an annual report of trade barriers around the world. These reports are based on complaints by US firms and not all issues are equally important, but they do provide a comprehensive overview of measures that impede access to the EU market. With respect to the USTR's list of complaints, I have not included measures that are either not regulatory in nature (e.g., the presence of public monopolies) or do not directly impede trade (e.g., subsidies and the inadequate protection of intellectual property rights) or do not impede US firms (e.g., reciprocity requirements in banking, insurance and investment services). Again, I do not consider disputes (formal or otherwise) involving individual EU member states (see Table 2).

By using both the WTO and USTR sources to identify disputes, this paper substantiates the impression that a large proportion of regulatory trade barriers are not the subject of formal dispute settlement (see Table 2).

[Insert Table 2 about here]

### 4. The external impact of the single European market<sup>4</sup>

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<sup>4</sup> This section draws on the work I did with Chris Stevens as part of the 1996 Single Market Review, published as Commission, 1998b.

This section makes the case for expecting the EU's regulatory barriers to cluster in particular areas. This argument is supported by analyses of a few illustrative measures, which were selected from the sub-set of EU rules that have been identified as barriers to third-country imports.

The SEM is the world's most ambitious (and successful) project to tackle regulatory barriers to trade in goods (and services). Although the fear that the SEM would result in a 'fortress Europe' (USITC, 1993) has generally proved unfounded (Commission, 1998; WTO, 1995), in some instances the single market programme has exacerbated regulatory barriers to the EU market.

This differentiated external impact of the SEM is due to the EU's multi-track approach to market integration. Different modes of market integration are deployed to tackle different types of regulatory barriers. These different modes of market integration have different implications for imports.

### **Modes of market integration**

The EU has used essentially four modes of market integration (see Table 3). The successful application of the mutual recognition principle as a method of market integration is entirely positive for third-country firms as it provides access to the entire EU market on the basis of meeting one member state's rules. The mutual recognition principle assumes that although member states' rules might differ in substance, unless proved otherwise, they should be considered to be equivalent in effect. Consequently, the default scenario is for the member governments to accept products legally on sale in other member states. The assumption of equivalence is crucial, however. If a member government is not convinced that another country's measures are equivalent, it can exclude the product in question. Such a decision, however, is potentially subject to judicial review under EU law.

[Insert Table 3 about here]

Even within the relatively homogenous club of countries that is the EU, however, many national regulations cannot be assumed to be equivalent in effect. These products tend to be those that present higher risks. As a consequence, the EU has frequently engaged in 'positive integration' -- agreeing common rules -- in order to achieve market integration.

The least intrusive mode of 'positive integration' is the so-called 'new approach'. Under 'new approach' directives, the European institutions confine themselves to agreeing common 'essential requirements,' which establish only regulatory objectives, not the means of achieving them. Developing detailed specifications to meet these requirements is delegated to the European standards bodies.<sup>5</sup> Even European standards developed by these bodies, although bringing advantages, are not mandatory; any product that meets a standard that is certified as meeting essential requirements can circulate freely within the EU. Thus 'new approach' directives are also fairly benign to imports. As they set only required objectives, a foreign firm may be able to continue to use its national (or firm) standard so long as a notified third party certifies that this standard conforms with the essential requirements of the directive.

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<sup>5</sup> The European Committee for Standardisation (CEN), the European Committee for Electrotechnical Standardisation (CENELEC) and the European Telecommunications Standards Institute (ETSI). See <http://www.NewApproach.org>.

Third-country goods are most likely to face market access problems with regard to products that are subject to detailed harmonisation (Woolcock, 1991). This is not to say that regulatory approximation within the EU does not bring benefits to third country firms in terms of eliminating the need to comply with multiple national requirements and increasing transparency. However, although it is possible that the common rules may be less restrictive than the national ones they replace, the tendency, as I shall explain below, is for them to be stricter. As such rules also tend to be detailed, they are potentially very restrictive to trade. Note, for example, the high priority that US and EU leaders assigned to reducing barriers to trade in cars caused by different safety and emissions regulations in the 1995 'Joint EU-US Action Plan' (and the difficulty they have had in making progress).

Within the category of harmonised product regulations, rules that govern how products are produced present particular problems for third-country firms. As mentioned above, so-called 'process' regulations do not generally present barriers to trade, however, they can present a problem when the production process is considered to have altered the product. This seems to be a particular problem with respect to food safety. The EU-US WTO dispute over hormone-treated beef fits into this category, as do the simmering EU-US disputes over GM food, rBST milk, wine-making rules and anti-microbial treatments in poultry production.

The fourth mode of market integration employed in the EU is a common authorisation, which applies to individual products, not just to product categories. Forms of common authorisation currently apply to pharmaceuticals and genetically modified crops. Although such close regulation is very trade restrictive, having a single authorisation rather than multiple such authorisations should (in theory) be liberalising. This has been the case with pharmaceuticals, where a centralised authorisation procedure is based on a technical assessment by the European Medicines Evaluation Agency (EMA). The approval procedures for GM crops and food is more decentralised (and so has more veto points), and more politicised.<sup>6</sup> As a result approvals have been frozen since 1998, which creates problems for imports of crops and foods from countries with more approved GM varieties.

### **The dynamics of 'positive integration' and pressures for approximation**

When the EU adopts common rules the dynamics of market integration press for regulatory approximation at a strict level. The energy for approximation comes from member governments having the right, albeit within limits, to enforce national standards despite the mutual recognition principle and even when common rules have been agreed. Because, under EU law, a member government may be able to maintain stricter standards that impede trade, there are incentives for its trading partners to either adapt (at firm level) or to negotiate a common rule (Vogel, 1995; Young and Wallace, 2000).

When common rules are negotiated, the government with legitimate, stricter standards is in a strong bargaining position because the costs of no-agreement fall more heavily on its trading partners, whose firms are excluded from its market, while its firms are shielded from competition (Fisher and Ury, 1982; Garrett and Tsebelis, 1996). This creates a political dynamic that favours the adoption of stricter common standards.

#### *Pressure for approximation*

Progress on trade liberalisation within the EU has been possible only because the institutional framework acknowledges and respects the member governments' prerogative to pursue legitimate public policy objectives,

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<sup>6</sup> For a fuller discussion see Young (2001).

even at the expense of interfering with the free movement of goods, services, capital and people (Young and Wallace, 2000). This acceptance of legitimate national restrictions provides the catalyst for approximation of regulations at stricter standards.

The mutual recognition principle, particularly the assumption that different national measures are equivalent in effect, has been questioned numerous times. Many of these exclusions have not stood up to legal scrutiny, but many others have. Significantly, the ECJ has not required governments to provide conclusive proof that a product would harm human health before it can exercise its prerogative under Article 30 (ex-36) to prohibit it (Weatherill and Beaumont, 1993). This was illustrated in the *Eysen* case, in which the Dutch government's ban on the preservative nisin in processed cheese was challenged as an unfair trade barrier. Although existing scientific evidence on the health risk of nisin was equivocal, the ECJ took the view that a government is entitled to protect its public from substances the safety of which is subject to scientific doubt.<sup>7</sup>

Legitimate restrictions aside, mutual recognition does not appear to be working as well in practice as it should in principle (Commission, 1999). The problem is particularly acute with respect to foods, electrical engineering, construction products, cars, financial services and professional qualifications. Although the EU, at least with respect to food,<sup>8</sup> has sought to facilitate mutual recognition by approximating the concepts, principles and procedures used by national regulatory agencies. Such attempts to approximate practice are relatively recent and are limited to only a few product areas. More common is for the EU to respond to persistent regulatory barriers among its member states by seeking to agree common rules.

#### *Pressure for stricter standards*

When one country has stricter product regulations than another, its relevant industry is protected while that of its trading partner is hurt. In the context of an international institution committed to eliminating technical barriers to trade, such as the EU, this is highly likely to lead to 'trading up,' as numerous studies have illustrated (Peterson, 1997; Sbragia, 1993; Scharpf, 1996; Vogel, 1993, 1995; Young and Wallace, 2000). The dynamic is particularly powerful when it intersects with an 'advocacy alliance' involving civic interest groups and the European Commission and/or European Parliament (Young and Wallace, 2000: 21-24). This dynamic has influenced much of the approximation of EU legislation and the establishment of centralised authorisation procedures.

Several of the current serious trade disputes with the US, including those over hormone-treated beef and GM food, were at least exacerbated by the dynamic of 'trading up.' When the use of hormones in rearing beef became an issue in the early 1980s there were five artificial and natural hormones in use.<sup>9</sup> Six of the then 12 member governments banned all five, while the other six authorised the use of at least one, including the British and Irish governments, which permitted all five. Because the EU's institutional framework permits qualified majority voting, the Council of Ministers was able to adopt a general ban in December 1985, despite British, Danish opposition (and Irish abstention).

Further, even when common EU product standards have been adopted, it is possible, under certain circumstances and with the prior approval of the Commission, for member governments to impose more stringent national standards under Article 95(5) (ex-100a(4)). This provision was originally incorporated into the

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<sup>7</sup> I am grateful to Peter Holmes for bringing this case to my attention.

<sup>8</sup> See, for example, the new food safety regulation (178/2002/EC) and the revised directive on GM crop approvals (2001/18/EC).

<sup>9</sup> This account is based on Vogel (1997: 15-17) and Princen (2002: 141-3).

1987 Single European Act in order to address the Danish and German governments' concerns that single market rules adopted under qualified majority voting, with them in the minority, might force them to accept products that they consider unsafe or environmentally harmful (Ehlerman 1987).

A number of pieces of secondary legislation contain analogous escape clauses that permit member governments to diverge from the common policy under specified circumstances. Such provisions provide scope for the dynamics of 'trading up' to continue to press for even stricter standards even after common rules are adopted. Such dynamics shaped, for example, the revision of the EU's procedures for approving genetically modified crops.<sup>10</sup> During 1997-98 the Austrian, French, Greek and Luxembourg governments invoked the 'safety clause' (Article 16) of Directive 90/220/EEC to ban the sale of even EU approved varieties of GM crops. Frustration at the resulting fragmentation of the single market gave impetus to the Commission's reform efforts (Commission, 1998a). The Danish, French, Greek, Italian and Luxembourg governments kept up the pressure for reform, by declared that they would not approve any new GM crops until a revised directive was adopted (Council, 1999). The new directive is stricter than the one it replaces in several respects; it places greater emphasis on precaution and environmental risk assessment; limits consents to 10 years (which may be extended upon review); and requires tracability, monitoring, and labelling throughout the production process.

#### *Protection or protectionism?*

The dynamic of 'trading up' means that the approach of the most cautious<sup>11</sup> member government is likely to be reflected in any common EU rule. Further, because much EU regulation with respect to risk is the product of negotiation, it tends to be inherently political. These related features of EU regulatory approximation are a potent source of trade tension with the United States as they amplify differences in regulatory approaches between the EU and US.

In the US regulatory responsibility is delegated to (technical) independent agencies -- most notably, the Environmental Protection Agency and the Food and Drug Administration. US regulatory agencies must follow procedural requirements laid down by Congress, and by law their final regulations must be justified by policy rationale, scientific bases and legal authority (US, 2000). In addition, US regulatory decisions are subject to legal review and often end in litigation (Jasanoff, 1987). These two features combine to lead agencies to base decisions closely on scientific evidence (Andersen, 1999; Vogel, 2000).

The sharp differences in regulatory approaches between the EU and US has been an important source of trade tensions (Vogel, 1997; 2001; Woolcock, 1991). A significant proportion of the US government's objections to EU regulations are rooted in such different attitudes towards risk management (see Table 4).

[Insert Table 4 about here]

#### 5. Considered multilateralism?

Although the United States government makes extensive use of the WTO's dispute settlement mechanism, accounting for nearly a quarter of all cases, strikingly the US government has pursued very few cases involving profound differences in regulatory approach. It has pursued only one such case against the EU (see Table 4) and

<sup>10</sup> For a fuller discussion, see Young, 2001, 9-14.

<sup>11</sup> It is worth noting that this involves caution with respect to new risks, it does not necessarily mean that existing risks are not actually more serious. I am grateful to Daniel Esty for stressing this point.

initiated one other; against Australian restrictions on salmon imports. This reticence is not unique to the US. Including the US cases on hormone-treated beef and salmon and two cases brought by the Canadian government on the same issues, through mid-2002 less than 4 percent of WTO cases have involved substantive regulatory differences.<sup>12</sup>

A crucial reason why the US government and others have been cautious about prosecuting foreign rules reflecting profound differences concerning regulatory objectives is that they might not win. The WTO, as the EU, does not unequivocally favour free trade. Rather it sets limits on the exceptions to free trade.<sup>13</sup> Although commonly ignored, this should not come as a surprise. The WTO Agreements were, after all, negotiated by governments that, while keen to remove others' protectionist practices, did not want to restrict their ability to adopt necessary protective measures.

Consequently, Article XX of the 1947 General Agreement on Tariffs and Trade (incorporated into the WTO) recognises the protection of human, animal or plant life or health as legitimate objectives for government action that may impede trade, so long as the measures in question are not a means of arbitrary discrimination between countries or disguised restrictions on trade. A WTO Dispute Settlement Panel, for example, interpreted Article XX in such a way that even though the French government's prohibition on asbestos fibres and asbestos products was discriminatory, it was justified under GATT Article XX (WTO, 2000b). The Appellate Body reversed this decision and declared that the French ban on all sales of asbestos, imported or not, was not a trade barrier.<sup>14</sup> Further, although the WTO's DSB famously ruled against the US ban on shrimp imported from countries that do not demonstrate that their shrimp trawlers match US efforts to protect sea turtles, it criticised the means not the ends. In fact, a subsequent panel, asked whether the changes to US policy were adequate, accepted that as applied the US's revised guidelines, even though they violated GATT Article XI.1, were justified under Article XX so long as the US government was engaged in good-faith efforts to reach a negotiated multilateral solution (Commission, 2001).

The WTO's Technical Barriers to Trade (TBT) Agreement – which covers, *inter alia*, labelling – and the Sanitary and Phytosanitary (SPS) Agreement – which specifically deals with regulations affecting agricultural products and food – also recognise protecting consumers and the environment as a legitimate reasons for a government to adopt trade-impeding regulations, although subjecting them to procedural disciplines.<sup>15</sup> In particular, both agreements allow governments a fair degree of leeway in pursuing their policy objectives, particularly with respect to the level of risk that they are willing to accept (Commission, 2000a; PIU, 2000; WTO, 1998: para 253j).

The one WTO case concerning differences of opinion concerning the nature of the risk that the US government has initiated against the EU concerned the EU's ban on hormone-treated beef (WT/DS26). The Appellate Body of the WTO overturned the EU's ban of six hormones on the grounds that the decision to ban them was not based on an appropriate risk assessment (Isaac, Banerji and Woolcock, 2000: 228). The Appellate Body's decision, however, clarified that political systems can manage identified risks as they see fit (Commission, 2000a).

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<sup>12</sup> As of 17 June 2002 there had been 10 such cases out of a total of 259 cases had been opened, of which four of these had been dropped and reopened or not pursued.

<sup>13</sup> I am grateful to Peter Holmes for putting this insight so succinctly.

<sup>14</sup> I am grateful to Peter Holmes for setting me straight on this.

<sup>15</sup> For a fuller discussion, see PIU (2000).

Significantly, the EU's ban on hormone-treated beef was a particularly poorly founded regulation. As Table 4 confirms, no other US-EU differences of opinion concerning risk have not gone to formal dispute settlement, although the US has begun making threatening noises about initiating proceedings against the EU's moratorium on GM foods and has raised the EU's rules in the WTO's TBT and SPS Committees.<sup>16</sup> Most irritations, however, have persisted for quite some time, without resolution (see Table 5).

[Insert Table 5 about here]

The second major reason why there have been relatively few WTO cases involving profound differences in regulatory approach is that even a legal victory may not bring policy change.<sup>17</sup> Because the trade-impeding rule stems from different regulatory approaches, it is reasonable to assume that such a rule might be more difficult to change than more traditional trade measures. Changing or removing a regulatory measure does much more than affect the price of competing imports, as is the case with tariffs. It may well affect the production requirements for even non-trading firms. Further, while tariff reductions bring unalloyed gains to consumers in lower prices, trade liberalisation through easing of regulatory barriers may involve exchanging price for safety. Both of these factors, arguably, make finding the political trade-offs between importers and exporters much more difficult (Holmes and Young, 2001b). Revising regulations is particularly difficult in the EU, where any common rule is the product of lengthy and complex negotiations and often embodies a finely balanced compromise.

It is, therefore, not surprising that the EU has been the only political system targeted with sanctions for failing to comply with adverse WTO judgements: banana trade regime (US) and the ban on hormone-treated beef (US and Canada). In the two other cases in which sanctions have been authorised -- Ecuador against the EU for bananas and Canada against Brazil for export subsidies in aircraft -- the winning country did not exercise its rights (Charnovitz, 2002). Even under the pressure of sanctions, the EU has been slow to change its rules. The EU and US reached an agreement to settle the bananas dispute in April 2001, nearly five years after the WTO panel was established and two years after the imposition of sanctions. More than five years after the WTO Appellate Body found against the EU's ban on hormone-treated beef and three years after the imposition of sanctions, the EU shows no sign of lifting its ban.

There are some additional, broader considerations that also mitigate against aggressively pursuing legal action against politically sensitive regulations. First, a finding by the WTO's dispute settlement body sets precedents, and government officials have to be alert to the implications of an apparently favourable ruling for domestic regulators (Shaffer, 2001).<sup>18</sup> A successful case that establishes a precedent that undesirably constrains domestic policy might be considered a pyretic victory. The US government, for example, appealed against the

<sup>16</sup> Bridges: Trade BioRes, 2/1, 24 January 2002 <http://www.ictsd.org/02-01-24/story1.htm>, accessed 6/2/02; European Council Regulation No. 1139/98 Compulsory Indication of the Labelling of Certain Foodstuffs Produced from Genetically Modified Organisms: Submission by the United States' G/TBT/W/94, 16 October, 1998 (WTO Committee on Technical Barriers to Trade); Sanitary and Phytosanitary Measures Committee 31 October-1 November 2001, [http://www.wto.org/english/news\\_e/news01\\_e/ss\\_nov2001\\_e.htm](http://www.wto.org/english/news_e/news01_e/ss_nov2001_e.htm) (accessed 6 November 2001).

<sup>17</sup> Interviews with representatives of the European-American Business Council (Washington, DC, 8 Jan. 2001), the National Food Processors Association (Washington, DC, 9 Jan. 2001); and the US Grains Council (Washington, DC, 11 Jan. 2001).

<sup>18</sup> Interview with a USDA official, Washington, DC 11 Jan. 2001.

favourable judgement in its case on Japanese taxes on alcoholic beverages (WT/DS11) because it found the Dispute Settlement Body's interpretation of the multilateral trade rules too broad (Wille, 1997) and therefore potentially more constraining on domestic regulatory autonomy. Second, there is a strong disincentive to unsettle unnecessarily relations with an important political ally and economic partner (Shaffer, 2001). Third, a number of politically influential firms with extensive operations on both sides of the Atlantic dislike trade disputes between the EU and US because even when they are not directly affected they suffer from the poisoned atmosphere.<sup>19</sup> Lastly, there is a desire not to further strain the WTO dispute settlement mechanism by giving it another politically charged case that might further undermine the already challenged legitimacy of the multilateral trading system (Holmes and Young, 2001b).

## 6. Conclusions

This paper argues that an increasingly important aspect of the EU's trade policy is the external impact of internal rules adopted for regulatory rather than trade reasons. The most trade-impeding of these rules tend to cluster where the regulatory differences, particularly with regard to risk management, among the member states are most pronounced.

Trade-barriers stemming from such measures are particularly difficult to resolve for two reasons: 1) they may not contravene international rules and 2) there is particularly strong political resistance to policy change. Trade barriers stemming from the EU's regulation of risks may not contravene multilateral rules, because those rules strike a balance between permitting protection and prosecuting protectionism. Such exceptions to free trade are a necessary part of the deal for making extensive behind-the-border liberalisation politically acceptable. In this sense they are an extension of the compromise of 'embedded liberalism' between liberal internationalist orthodoxy and domestic interventionism that permitted the creation of the Bretton Woods System (Ruggie, 1982: 209). This paper, while preliminary and unrepresentative, suggests that both EU and WTO rules favour letting a guilty party go free rather than convicting an innocent. Consequently, governments retain a significant degree of regulatory autonomy despite deeper integration.

Even where the EU's measures contravene international rules, the EU has often been resistant to policy change. Although this paper has focused on the EU, such resistance to policy change is not unique to the EU and may be common to more divided systems of government, of which the United States is the other prime example. Political resistance to change and the trade-barriers' roots in profoundly different regulatory approaches mean that negotiated solutions to such trade barriers are highly unlikely. Although governments readily resort to the WTO's binding dispute settlement proceedings in many areas, with respect to such politically sensitive issues they proceed with considerable caution.

The related combination of legitimate exceptions to free trade and the cautious prosecution of some regulatory trade barriers by governments mean that a degree of trade friction will be an enduring feature of international trade. Thus 'system friction' would seem to be an inevitable consequence of deeper integration. Arguably, this is not too heavy price to pay for political acceptance of the project of further trade liberalisation.

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<sup>19</sup> Comment by Sir John Browne, European University Institute, 10 November 2000. See also the 'EU Committee Position Paper on the Implications of Agro-Food Developments on International Trade and Transatlantic Relations,' <http://www.eucommittee.be/pop/pop1997/Agf/agf4.htm>, 1 December 1997. One of the TABD's priority issues for 2001 is 'Dispute Management', which includes resolving existing disputes and avoiding new ones (*TABD Newsletter*, February/March, 2001).



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**Table 1 WTO cases brought by the US against the EU, 1995-mid-2002**

(excludes cases brought against individual member states)

| <i>Case</i>                                                                                                                      | <i>Consultation</i> | <i>Panel</i> | <i>Status</i>                                                                                                            |
|----------------------------------------------------------------------------------------------------------------------------------|---------------------|--------------|--------------------------------------------------------------------------------------------------------------------------|
| <b>WT/DS13</b><br>Duties on imported grains                                                                                      | 7/95                | 3/97         | Negotiated agreement (11/95)<br>Request for panel withdrawn following implementation (4/97)                              |
| <b>WT/DS16</b><br>Import regime for bananas<br>(brought with Guatemala, Honduras and Mexico)                                     | 10/95               | --           | Dropped and reopened as DS27 with a wider set of articles invoked and with the addition of Ecuador as a complainant.     |
| <b>WT/DS26</b><br>Ban on meat and meat products that have been treated with growth hormones.                                     | 1/96                | 4/96         | Appellate Body found in favour of US (2/98)<br>Sanctions in place.                                                       |
| <b>WT/DS27</b><br>Import regime for bananas<br>(DS13, but with more articles invoked and Guatemala as a complainant)             | 2/96                | 4/96         | Appellate Body found in favour of the plaintiffs (9/97)<br>EU adopted revised rule (7/98)                                |
| <b>WT/DS62</b><br>Custom classification of some computer equipment raised tariff                                                 | 11/96               | 2/97         | Appellate Body overturned Panel report favouring US (6/98)                                                               |
| <b>WT/DS104</b><br>Export subsidies - processed cheese                                                                           | 10/97               | --           |                                                                                                                          |
| <b>WT/DS124</b><br>Enforcement of intellectual property rights for motion pictures and television programs in Greece             | 5/98                | --           | Negotiated solution (3/01)                                                                                               |
| <b>WT//DS158</b><br>Import regime for bananas II                                                                                 | 1/99                |              | Compliance panel found revised EU regime still incompatible (4/99)<br>Sanctions imposed.<br>Negotiated settlement (4/01) |
| <b>WT/DS172</b><br>Commission approval of a preferential French government loan to develop a flight management system for Airbus | 5/99                | --           |                                                                                                                          |
| <b>WT/DS174</b>                                                                                                                  | 6/99                | --           |                                                                                                                          |

|                                                                                                                       |      |    |  |
|-----------------------------------------------------------------------------------------------------------------------|------|----|--|
| No national treatment protection for trademarks and geographical indications for agricultural products and foodstuffs |      |    |  |
| <b>WT/DS/223</b><br>Tariff-rate quota on corn gluten feed                                                             | 1/01 | -- |  |

Note: Columns 'Consultation' and 'Panel' report date requested.

Source: WTO dispute database ([http://www.wto.org/english/tratop\\_e/dispu\\_e/dispu\\_status\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm)), accessed 18 and 20/2/02.

**Table 2 Main US concerns about EU rules**

| <i>Type of barrier</i>                   | <i>Measure</i>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
|------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Border measures                          | BANANAS (tariff quota + discriminatory licensing) (agreement 4/01)<br>IMPORTED GRAINS (agreement (11/95)<br>CUSTOMS CLASSIFICATION OF COMPUTER EQUIPMENT (in EU's favour 6/98)<br>TARIFF-RATE QUOTA ON CORN GLUTEN FEED                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| Regulatory barriers to trade in goods    | HORMONE-TREATED BEEF<br>HUSHKITS (dispute brought to ICAO)<br>Lack of national treatment with respect to GEOGRAPHICAL INDICATIONS for agricultural products and foods<br>Lack of national treatment with respect to geographical indications for wines and spirits<br>Ban on milk produced using recombinant bovine somatotropin (rBST)<br>Ban on some antimicrobial treatments in poultry production<br>Effective moratorium on approval of GM products since 4/98<br>Mandatory labelling of all foods containing more than 1% GM ingredients<br>Ban on food, feed and fertiliser containing specified risk materials<br>Treatment and tracability of raw materials used in gelatine for human consumption<br>Derogation from EU standards required for US wine (negotiations underway)<br>Heat or pressure treatment of softwood packing material<br>Slow and arbitrary new aircraft certification<br>Labelling of TSP (fertiliser) disadvantages US exports<br>Testing of pharmaceuticals at point of entry |
| Regulatory barriers to trade in services | European content requirements for TV broadcasts                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |

Notes: Excludes measures not in effect

Omits systemic barriers, government procurement, intellectual property protection, subsidies.

Small caps denotes that formal WTO proceedings have been initiated

Source: adapted from USTR (2001; 2002).

**Table 3 Modes of market integration in the EU**

| <i>Mode</i>                  | <i>Description</i>                                              | <i>Estimated share of intra-EU trade accounted for by affected products</i> |
|------------------------------|-----------------------------------------------------------------|-----------------------------------------------------------------------------|
| Mutual recognition principle | Different national standards assumed to be equivalent in effect | 30%                                                                         |
| 'New approach'               | Common objectives with reference to voluntary standards         | 20%                                                                         |
| Approximation                | Common detailed rules                                           | 30%                                                                         |
| Common authorisation         | Common approval of individual products required                 | pharmaceuticals<br>GM crops and food                                        |

Notes: Percentages do not add to 100 because not all products are subject to product-specific regulation

Source: Adapted from Holmes and Young (2001a) and Commission (2002).

**Table 4 US regulatory disputes with the EU**

| <i>Status of dispute</i>                                                    | <i>Perception of measure</i>                                                                                                                                                                                                                |                                                                       |                                                |
|-----------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------|------------------------------------------------|
|                                                                             | <i>Measure not warranted</i>                                                                                                                                                                                                                | <i>Agree with objective, but not means</i>                            | <i>Protectionist</i>                           |
| multilateral dispute settlement proceedings (formal consultation initiated) | ban on hormone-treated beef                                                                                                                                                                                                                 | rules excluding the use of hushkits                                   |                                                |
| Simmering dispute                                                           | moratorium on approvals of GM crops and foods<br>labelling requirements for GM foods<br>ban on rBST milk<br>ban on some anti-microbial treatments in poultry production<br>labelling of TSP fertiliser<br>limits on low frequency emissions |                                                                       | European content requirement for TV broadcasts |
| Agreement negotiated or reported near                                       |                                                                                                                                                                                                                                             | wine-making rules<br>rules on treatment of softwood packing materials |                                                |

|  |  |                                                                                                                         |  |
|--|--|-------------------------------------------------------------------------------------------------------------------------|--|
|  |  | data privacy requirements<br>treatment and tracability<br>of raw materials used<br>in gelatine for human<br>consumption |  |
|--|--|-------------------------------------------------------------------------------------------------------------------------|--|

Note: Perception of measure is inferred from descriptions by the USTR.

Source: Based on USTR (2001; 2002).

**Table 5 Persistent disputes involving profound differences about risk management**

| <i>Dispute</i>                                | <i>Issue since...</i>                                 | <i>Status</i>                                              |
|-----------------------------------------------|-------------------------------------------------------|------------------------------------------------------------|
| Ban on hormone-treated beef                   | Ban 1/89<br>WTO consultation 5/96                     | WTO case favouring US, measure still in place              |
| Approval of GM foods                          | Last approval 4/98<br>Raised in SPS Committee 11/01   | Under discussion in SPS Committee                          |
| Labelling of GM foods                         | Novel Foods Dir. 5/97<br>Raised in TBT Committee 7/98 | Under discussion in TBT Committee                          |
| Ban on rBST milk                              | Moratorium extended 12/94                             | 3 unsuccessful attempts to reach agreement in <i>Codex</i> |
| Ban on some anti-microbial poultry production | US exports blocked since 4/97                         | Negotiations on non-chlorine treatments                    |
| Labelling of TSP fertiliser                   | 1976                                                  | Scientific justification requested                         |

Source: USTR 1995, 2002